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Washington, DC 20405

JUN 1 1996

June 12, 1996

Mr. William F. Caton
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Federal Communications Commission
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DOCKET FILE COPY ORIGINAL

Subject: Allocation of Costs Associated with Local Exchange Carrier
Provision of Video Programming Services, CC Docket No. 96-112

Dear Mr. Caton:

Enclosed please find the original and eleven copies of the General Services Administration's Reply Comments for filing in the above-referenced proceeding. Copies of this filing have been served on all interested parties.

Sincerely,

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Enclosures

cc: International Transcription Service
Andrew Mulitz (Diskette and copy)
Ernestine Creech

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**BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554**

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JUN 17 1996

In the Matter of)
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Allocation of Costs Associated with)
Local Exchange Carrier Provision of)
Video Programming Services)
_____)

CC Docket No. 96-112

**REPLY COMMENTS OF THE
GENERAL SERVICES ADMINISTRATION**

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June 12, 1996

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Summary

In these Reply Comments, GSA joins the state commissions and other users of telephone services in supporting the Commission's cost allocation proposals. These carefully crafted proposals will promote fair competition in the video market and ensure just and reasonable telephone rates.

GSA agrees with the non-LEC parties that all LECs should be required to follow the Commission's cost allocation rules, regardless of the interstate price cap election they happen to make in any particular year.

GSA also agrees with the non-LEC parties that the Commission should prescribe a fixed factor for the allocation of shared plant in the outside plant accounts. GSA supports an allocation of from 50 to 75 percent of shared outside plant facility costs to video.

GSA also agrees with the non-LEC parties that the Commission should require the direct assignment of spare capacity whenever possible. GSA concurs in the recommendation of most parties that maintenance expense be allocated in proportion to maintained plant.

Finally, GSA agrees with the non-LEC parties that reallocations of plant from regulated to nonregulated should be treated as price cap exogenous factors. In this way, telephone ratepayers will benefit from the economies of scope possible through the provision of video services over an integrated network.

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CC Docket No. 96-112

**REPLY COMMENTS OF THE
GENERAL SERVICES ADMINISTRATION**

The General Services Administration ("GSA"), on behalf of the Federal Executive Agencies, submits these Reply Comments in response to the Commission's Notice of Proposed Rulemaking ("NPRM"), FCC 96-214, released May 10, 1996. In this NPRM, the Commission requested comments and replies on the allocation of costs associated with the provision of video programming services by local exchange carriers ("LECs").

I. Introduction

On May 28, 1996, GSA filed Comments commending the Commission for initiating this proceeding to ensure that ratepayers pay telephone rates that are just and reasonable.¹ GSA recommended that the Commission allocate over 50 percent of the cost of shared broadband network costs to nonregulated to prevent the cross-subsidization of LEC video ventures by telephone ratepayers.

¹ Comments of GSA, p. 3.

Comments were also filed in this proceeding by:

- The United States Telephone Association (“USTA”) and thirteen LECs and LEC representatives;
- The National Cable Television Association, Inc. (“NCTA”) and six individual cable television operators (collectively, the “Cable Parties”);
- Four public service commissions
- Three interexchange carriers.
- The Pennsylvania Office of Consumer Advocate (“PaOCA”); and
- BroadBand Technologies, Inc. (“BroadBand”).

In these Reply Comments, GSA responds to the comments and recommendations of these parties.

II. The Commission’s Price Cap Plan Does Not Reduce The Need For Proper Cost Allocation.

USTA and a number of LECs argue that the Commission’s Part 64 cost allocation rules are not necessary for LECs electing the Commission’s “no sharing” price cap option.² Cox Communications, Inc. (“Cox”) and various other parties provide sound reasons for the rejection of these arguments.³ The Commission should reject this argument out of hand.

² See, e.g., Comments of USTA, pp. 4-6; Southern New England Telephone Company (“SNET”), pp. 3-5; Pacific Bell and Nevada Bell (“Pacific”), pp. 3-5; Sprint Local Telephone Companies (“Sprint”), pp. 4-5.

³ See, e.g., Comments of Cox, pp. 11-12; AT&T Corp. (“AT&T”), pp. 11-12; Comcast Cable Communications, Inc. and Adelphia Communications Corporation (“Comcast/Adelphia”), p. 9; Alabama Public Service Commission (“Alabama”), p. 8.

First of all, the Communications Act of 1934, as amended (“Communications Act”), specifically requires the Commission to prescribe a system of accounting methods, procedures, and techniques which shall ensure a proper allocation of all costs.⁴ Furthermore, the Telecommunications Act of 1996 (“1996 Act”)⁵ added a requirement that the Commission and state commissions “establish any necessary cost allocation rules, accounting safeguards, and guidelines to ensure that services included in the definition of universal service bear no more than a reasonable share of the joint and common costs of facilities used to provide those services.”⁶ The Commission’s accounting responsibilities are thus entirely separate from its interstate tariffing responsibilities, and must be performed pursuant to law regardless of any procedures, such as price caps, which it employs in the regulation, or deregulation, of interstate rates.

Second, 75 percent of the regulated cost of subscriber loops, the principal subject of concern in this proceeding, is allocated to the intrastate jurisdiction pursuant to the Commission’s Part 36 rules.⁷ A LEC’s election of the interstate “no sharing” option does nothing whatsoever to protect intrastate ratepayers from improper cost allocations.

Finally, under the Commission’s current price cap plan, LECs are free to elect to return to sharing in any year. Even were the Commission to eliminate all sharing options, it is certain that the LECs would remain subject to productivity offsets and periodic reviews

⁴ Communications Act, Section 220(a)(2).

⁵ Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996).

⁶ 1996 Act, Section 254(k).

⁷ 47 C.F.R. § 36.154.

of the price cap plan results. If LEC regulated costs were inflated by the costs of nonregulated activities, industry productivity and financial results would be seriously distorted to the detriment of telephone ratepayers.

In summary, it is of critical importance that the Commission require all LECs, regardless of their interstate price cap election, to follow its Part 64 cost allocation rules.

III. The Commission Should Adopt A Fixed Allocator For Shared Outside Plant Accounts.

USTA and most LECs oppose the Commission's proposal to allocate shared outside plant costs according to a fixed allocator.⁸ Virtually all other parties to this proceeding support the Commission's proposal.⁹

Many LECs contend that a fixed factor is inappropriate because of variations in LEC network architecture, technology and deployment plans.¹⁰ GSA submits that such differences are not relevant to the use of a fixed factor for shared plant. Under the Commission's Part 64 rules, plant which can be directly assigned to either regulated or nonregulated is so assigned, and this methodology captures the effect of differences in LEC networks. The outside plant facilities which are used for both regulated and

⁸ See, e.g., Comments of USTA, pp. 6-12; GTE Service Corporation and its affiliated domestic telephone, wireless and video companies ("GTE"), pp. 6-9; Ameritech Operating Companies ("Ameritech"), pp. 19-21.

⁹ See, e.g., Comments of NCTA, pp. 4-15; AT&T, pp. 4-6; People of the State of California and the Public Utilities Commission of the State of California ("California"), p. 4.

¹⁰ See, e.g., Comments of BellSouth Corporation and BellSouth Telecommunications, Inc. ("BellSouth"), pp. 17-22; GNVW Inc./Management ("GNVW"), pp. 3-6; Harris, Skrivan & Associates, LLC ("HSA"), pp. 3-4.

nonregulated purposes are the only ones to which the fixed allocator would be applied.

Some LECs propose that shared plant be allocated in proportion to the directly assigned plant in each account.¹¹ While such a procedure might be reasonable if most plant is directly assigned and shared plant is *de minimis*, it is not reasonable in other circumstances. Experience with video dialtone applications has shown that common facilities predominate in integrated broadband networks.¹² The use of dedicated plant as a common facility allocation method is subject to gross manipulation in the context of integrated broadband networks, and should not be allowed by the Commission. As the Commission noted in its review of Bell Atlantic's video dialtone tariff, "if Bell Atlantic had been unable to identify any dedicated video dialtone costs in the shared portion of its distribution system, the result would have been a zero percent allocation of common costs to video dialtone."¹³

Other LECs propose that shared plant be allocated in proportion to video and telephone subscribers or revenues.¹⁴ Such methods would ensure that telephone ratepayers provide a massive subsidy to the start-up of LEC video operations. The construction of a broadband network to provide both video and telephone services creates

¹¹ See, e.g., Comments of Bell Atlantic, p. 9; Pacific, p. 9; Southwestern Bell Telephone Company ("SWBT"), p. 11.

¹² NCTA, p. 8; Comcast/Adelphia, pp. 5-6; MCI Telecommunications Corporation ("MCI"), p. 12.

¹³ Bell Atlantic Telephone Companies, Revisions to Tariff F.C.C. No. 10, Rates, Terms, and Regulations, Transmittal Nos. 741, 786, Order, DA 95-1285, released June 9, 1995, para. 33.

¹⁴ See, e.g., Comments of Puerto Rico Telephone Company ("PRTC"), pp. 9-10; U S West, Inc. ("U S West"), p. 10; NYNEX Telephone Companies ("NYNEX"), p. 11.

a fixed cost which would not be incurred at all in the absence of a video venture. The use of a subscriber or revenue based allocator would cause virtually all of these fixed costs to be assigned to regulated, at least in the early years. Such a deviation from cost causation principles must not be permitted by the Commission.

A fixed allocator, however, enables the Commission to ensure that telephone ratepayers will not be forced to subsidize LEC video ventures. MCI summarizes the benefits of a fixed allocator as follows:

- it recognizes the nontraffic sensitive nature of loop (and transport) facilities,
- its implementation would impose a minimum amount of administrative cost on ILECs and the Commission, and
- a fixed allocator can be selected that is consistent with cost causation principles, thereby protecting ratepayers.¹⁵

The Alabama Public Service Commission ("Alabama") adds:

The Commission has used this methodology, as noted in the NPRM, to allocate loop cost and other costs between jurisdictions. Those decisions were based on extensive work by both the Commission and state regulators through the joint board process and upheld by the United States Court of Appeals for the District of Columbia Circuit.¹⁶

GSA urges the Commission to adopt a fixed allocator for all shared outside plant accounts.

¹⁵ Comments of MCI, p. 8.

¹⁶ Comments of Alabama, p. 5.

IV. The Commission Should Allocate Over 50 Percent Of Shared Outside Plant to Nonregulated.

Some LECs proposed fixed factors which would allocate more shared outside plant costs to telephone than to video.¹⁷ These recommendations were based upon ratios of dedicated plant, subscribers, or revenues. However, as discussed above, such allocation methods are fatally flawed.

The Cable Parties supported factors which would allocate about 75 percent of shared outside plant costs to video.¹⁸ GSA finds the support for these recommendations highly credible. The Cable Parties present sound economic evidence that the incremental cost of video in an integrated system is about 75 percent of the total incremental costs.¹⁹ While any allocation of common costs is inherently controversial, an allocator based upon the ratio of incremental costs is at least reasonable. This is especially true when it is clear that an allocation based on actual or projected usage would attribute over 90 percent to video.²⁰ In this connection, GSA finds the explanation of bandwidth utilization in integrated systems provided by Continental Senior Vice President David M. Fellows to be especially

¹⁷ See, e.g., Comments of Bell Atlantic, p. 10; NYNEX, p. 15; PRTC, p. 3.

¹⁸ See, e.g., Comments of NCTA, pp. 15-21; Time Warner Cable ("TWC"), pp. 8-11; Cox, pp. 8-9.

¹⁹ See, e.g., Comments of NCTA, Attachment 1, pp. 4-6; Comcast/Adelphia, p. 7; California Cable Television Association ("CCTA"), pp. 17-20.

²⁰ Comments of GSA, p. 4; Continental Cablevision, Inc. ("Continental"), p. 5.

illuminating.²¹

An allocation of at least 50 percent to video is strongly supported by all four commenting state commissions, all three commenting IXC's, PaOCA and SNET.²² GSA urges the Commission to adopt a fixed factor which will allocate from 50 to 75 percent of the shared costs of outside plant accounts to video.

**V. Spare Facilities Should Be Directly
Assigned Whenever Possible.**

Many LECs oppose the Commission's proposal to establish separate cost pools to enable them to directly assign the costs of spare capacity.²³ The LECs argue that spare capacity is economically efficient and inherent in any network.

The Cable Parties and others support the Commission's proposal.²⁴ PaOCA states:

Spare capacity in recent years has run as high as 65% to 70%. Such spare capacity is not installed in anticipation of growth in telephone service, but for video service instead.²⁵

²¹ Comments of Continental, Affidavit of David M. Fellows.

²² See, e.g., Comments of Alabama, p. 6; California, p. 2; Florida Public Service Commission ("Florida"), p. 5; New York State Department of Public Service ("New York"), pp. 3-4; AT&T, p. 7; MCI, p. 15; General Communications, Inc. ("GCI"), p. 4; PaOCA, pp. 13-14; SNET, pp. 11-15.

²³ See, e.g., Comments of Bell Atlantic, pp. 13-14; BellSouth, p. 22; GTE, pp. 9-10.

²⁴ See, e.g., Comments of NCTA, pp. 6-7; PaOCA, pp. 15-16; Alabama, p. 7; GCI, pp. 5-6.

²⁵ Comments of PaOCA, p. 15 (footnotes deleted).

Alabama adds:

These spare facilities would appear to position the incumbent LECs very well to rapidly enter the video programming service at less costs. If these costs continue to be recovered from the regulated services it will create a distorted competitive environment for video programming service.²⁶

GSA recognizes that some spare capacity is economically efficient and reasonably allocatable along with utilized plant. The extreme level of spare capacity now being built by the LECs, however, raises legitimate concerns about the prudence and future use of these facilities. To ensure the integrity of the cost allocation process and just and reasonable rates for telephone ratepayers, the Commission should require the LECs to establish separate cost pools whenever a significant amount of spare capacity is engineered into their network in anticipation of the future provision of nonregulated video services. Because of the potential magnitude of misallocations in this area, the Commission should direct the LECs' independent auditors to certify specifically that they have reviewed this process as part of their annual Part 64 audit.

VI. Outside Plant Maintenance Expense Should Be Allocated On The Basis Of Network Investment.

NYNEX and SWBT oppose the Commission's proposal to allocate maintenance expense in proportion to the plant being maintained.²⁷ Both LECs would continue the current, usage-based allocation method.

²⁶ Comments of Alabama, p. 7.

²⁷ Comments of NYNEX, p. 17; SWBT, p. 18.

USTA, other LECs, AT&T and Alabama all recognize that usage-based maintenance allocators are not appropriate for fixed outside plant accounts.²⁸ Indeed, as noted above, if usage factors such as bandwidth or minutes were used, over 90 percent of the outside plant maintenance expense for integrated networks would be assigned to video. As NYNEX concedes, "Maintenance is largely a function of age, location, sensitivity to elements, etc."²⁹ Maintenance expense is thus logically allocatable to regulated and nonregulated in proportion to the plant being maintained.

VII. Reallocations Of Plant To Nonregulated Should Result In Exogenous Factor Reductions to LEC Price Caps.

USTA and some LECs oppose the Commission's proposal to require the LECs to reflect the effects of reallocations of plant from regulated to nonregulated as exogenous factors in their price cap filings.³⁰ Such factors would reduce LEC price caps.

The Cable Parties and IXC's strongly support the Commission's proposal.³¹ PaOCA states:

Any cost allocation adopted by the FCC will have no real effect unless the FCC applies this revision to rates. This adjustment is necessary to the price cap form of regulation so that the cost allocations discussed above are actually realized in prices that

²⁸ See, e.g., Comments of USTA, p. 19; Bell Atlantic, p. 12; AT&T, p. 9; Alabama, p. 6.

²⁹ Comments of NYNEX, p. 17.

³⁰ See, e.g., Comments of USTA, pp. 12-14; Pacific, pp. 16-18; Ameritech, pp. 7-8.

³¹ See, e.g., Comments of NCTA, pp. 23-24; Cox, pp. 10-11; Comcast/Adelphia, pp. 8-9; AT&T, pp. 10-11; MCI, pp. 16-17.

reflect those cost allocations.³²

Alabama adds:

Not requiring all price cap carriers to flow through to the regulated services the effects of the reallocation of cost would in fact protect competitors in competitive markets. It would also not comply with the requirements of the 1996 Telecommunications Act to assure that the basic services are not subsidizing the nonregulated competitive services.³³

The Commission should adopt its proposal to require LECs to reflect the reallocation of plant from regulated to nonregulated in their price cap filings.

³² Comments of PaOCA, p. 16.

³³ Comments of Alabama, p.8.

VIII. Conclusion

As the agency vested with the responsibility for acquiring telecommunications services on a competitive basis for use of the Federal Executive Agencies, GSA urges the Commission to revise its Part 64 rules to allocate from 50 to 75 percent of shared outside plant costs to nonregulated and make other such revisions as described herein.

Respectfully submitted,
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June 12, 1996

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I Michael J. Ettner do hereby certify that copies of the foregoing "Comments of the General Services Administration" were served this 12th day of June, 1996, by hand delivery or postage paid to the following parties:

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